

IRC Update¹

Revenue Laws Study Committee

April 2, 2008

Given the tremendous cost of conforming to recent changes to the Internal Revenue Code under the Economic Stimulus Act of 2008 (ESA), the Revenue Laws Study Committee recommends that the State "decouple" in some way. There are several ways in which to accomplish this result, some of which could actually result in a first-year revenue gain. However, the following are two revenue neutral options for the Committee's consideration:

Option #1:

Under this option, the depreciation rules and expensing deduction limits would be as if the Economic Stimulus Act had not passed.

Option #2:

Under this option, the State would not conform to the accelerated bonus depreciation schedule under the ESA, but it would conform to the increased expensing limits. To achieve revenue neutrality, the proposal would require taxpayers to add back to their State taxable income 85% of the amount the taxpayer deducted as bonus depreciation for federal purposes. Over the next five years, the taxpayer would be allowed to deduct the entire amount added back in five equal installments. This option is similar to the approach taken by North Carolina in 2002-2004 when Congress enacted bonus depreciation and increased expensing provisions following the September 11, 2001 attacks.

Code Provision	Option #1	Option #2	Full Conformity with ESA
Sec. 168(k) depreciation ("bonus depreciation")	<ul style="list-style-type: none">•Taxpayer must add back the amount taken as bonus depreciation.•Taxpayer may deduct the difference between what the regular depreciation would have been without the bonus depreciation less the actual regular depreciation taken on the federal return.	<ul style="list-style-type: none">•Taxpayer must add back 85% of the amount taken as bonus depreciation.•For succeeding 5 years, taxpayer may deduct addback amount in 5 equal installments.	Taxpayer may deduct 50% of the cost of property placed in service during 2008, the impact of which flows through to State net income.
Sec. 179 expensing	<ul style="list-style-type: none">•\$128,000 deduction.•Deduction begins to phase out when property reaches \$510,000.•Deduction phases out completely when property >\$638,000.	<ul style="list-style-type: none">•\$250,000 deduction.•Deduction begins to phase out when property reaches \$800,000.•Deduction phases out completely when property >\$1.05 million.	<ul style="list-style-type: none">•\$250,000 deduction.•Deduction begins to phase out when property reaches \$800,000.•Deduction phases out completely when property >\$1.05 million.
Estimated Impact:	- 0 -	- 0 -	(\$300 million)

¹ This proposal addresses conformity to and the fiscal impact of the Economic Stimulus Act only given its cost. Conformity to the other federal tax changes enacted since January 1, 2007 are estimated to cost \$1 million in FY0809 and \$2.3 million in FY0910.